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# Oil, Gas, and Mineral law

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# OIL, GAS, AND MINERAL LAW

Richard F. Brown \*

## TABLE OF CONTENTS

- I. INTRODUCTION
- II. TITLE AND CONVEYANCING ISSUES
- III. LEASE AND LEASING ISSUES
- IV. INDUSTRY CONTRACTS
- V. LITIGATION
- VI. REGULATION
- VII. CONCLUSION

## I. INTRODUCTION

This article focuses on the interpretations of and changes relating to oil, gas, and mineral law in Texas from November 1, 2012, through October 31, 2013. The cases examined include decisions of state and federal courts in the State of Texas and the Fifth Circuit Court of Appeals.<sup>1</sup>

## II. TITLE AND CONVEYANCING ISSUES<sup>2</sup>

*Key Operating & Equipment, Inc. v. Hegar*<sup>3</sup> held that a lessee's implied surface easement entitled the lessee to use a road across the surface of the leased tract to produce oil from any land pooled with the leased tract, so long as at least part of the purpose for using the road was to produce oil from the leased tract.<sup>4</sup> The

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1. This article is devoted exclusively to Texas law. Cases involving questions of oil, gas, and mineral law decided by courts sitting in Texas but applying laws of other states are not included. Page limitations of this publication required the omission of some cases of interest. The facts in the cases are sometimes simplified to focus on the legal principles.

2. Other notable cases dealing with title and conveyancing issues include the following: *Coates Energy Trust v. Frost Nat'l Bank*, No. 04-11-00838-CV, 2012 WL 5984693 (Tex. App.—San Antonio Nov. 28, 2012, pet. denied) (mem. op.) (three part deed construction); *Chesapeake Exploration, L.L.C. v. BNW Prop. Co.*, 393 S.W.3d 852 (Tex. App.—El Paso 2012, pet. denied) (conveyance of executive rights); *Dupnik v. Hermis*, No. 04-12-00417-CV, 2013 WL 979199 (Tex. App.—San Antonio Mar. 13, 2013, pet. denied) (mem. op.) (conveyance of surface only reserves minerals); *Key Prod. Co., Inc. v. Quality Operating, Inc.*, No. 10-10-00379-CV, 2013 WL 1286672 (Tex. App.—Waco Mar. 28, 2013, no pet.) (mem. op.) (depth limitation in designation of unit incorporated into subsequent assignment); *Meekins v. Wisnoski*, 404 S.W.3d 690 (Tex. App.—Houston [14th Dist.] 2013, no pet.) (sale of minerals subject to probate); *Thomason v. Badgett*, No. 02-12-00303-CV, 2013 WL 3488254 (Tex. App.—Fort Worth July 11, 2013, pet. denied) (mem. op.) (deed reservation construed against grantor).

3. *Key Operating & Equipment, Inc. v. Hegar*, 403 S.W.3d 318 (Tex. App.—Houston [1st Dist.] 2013, pet. granted).

4. *Id.* at 321.

Richardson Tract and the Curbo Tract were adjoining tracts.<sup>5</sup> Beginning in 1987, Key Operating leased and produced oil from the Richardson Tract.<sup>6</sup> In 1994, Key Operating acquired a lease on the Curbo Tract and built a road across the surface of the Curbo Tract to access oil wells on both tracts.<sup>7</sup> In 2000, the last well on the Curbo Tract stopped producing, and Key Operating acquired a new lease with a pooling clause on an undivided 1/16 of the minerals in the Curbo Tract.<sup>8</sup> Pursuant to the new lease, Key Operating pooled the Richardson and Curbo Tracts into the forty-acre Richardson-Curbo Unit.<sup>9</sup> The Unit included thirty acres from the Richardson Tract and ten acres out of the eighty-five acres in the Curbo Tract.<sup>10</sup> All production was from wells located on the Richardson Tract, which Key Operating accessed using the road across the Curbo Tract. In 2002, the Hegars purchased an unsevered 1/4 mineral interest and the surface of the Curbo Tract and built a house very close to the road.<sup>11</sup> Subsequently, Key Operating drilled a new well on the Richardson Tract that increased its use of the road.<sup>12</sup> In 2007, the Hegars sued Key Operating for trespass and sought a permanent injunction against Key Operating's continued use of the road. After a bench trial, the trial court permanently enjoined Key Operating from using the road for any purpose related to the production of minerals off the Curbo Tract.<sup>13</sup> The court entered a finding of fact that no minerals were being produced from the Curbo Tract.<sup>14</sup>

The Hegars advanced a number of theories on appeal that, if sustained, would have been very disruptive for the industry. The Hegars generally lost those points and the opinion is broadly supportive of the dominance of the mineral estate and the scope of the implied right to use the surface that is appurtenant to the mineral estate. Nevertheless, the Hegars won on a single factual sufficiency point, because there was no oil being produced from the Curbo Tract.<sup>15</sup>

The Hegars contended that the Key Operating lease and the pooling agreement did not exist prior to the original severance of the surface estate from the 1/16 of the mineral estate eventually leased by Key Operating and therefore were not in the Hegars' chain of title or binding on them.<sup>16</sup> The Hegars also contended that the rights of mineral owners to subsequently use the surface estate were limited to those rights that existed at the time of the mineral severance.<sup>17</sup> The court agreed that Key Operating's lease and pooling agreement, which are not part of the Hegars' chain of title and to which they did not agree,

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5. *Id.* at 323.

6. *Id.*

7. *Id.*

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.* at 324.

14. *Id.* at 333.

15. *Id.* at 336.

16. *Id.* at 324-25.

17. *Id.* at 324.

cannot expand Key Operating's right to use the Hegars' surface.<sup>18</sup> Under the common law, the owner or lessee of the dominant mineral estate has a right to develop the minerals, which includes "an implied right to use the surface estate in ways reasonably necessary to carry out its operations."<sup>19</sup> The mineral lessee's implied right to use the surface also generally extends to the surface of a pooled area, but a lease executed after the time the mineral and surface estates are severed is not part of the surface estate's chain of title and cannot bind subsequent surface estate owners without their consent.<sup>20</sup> Therefore, Key Operating could not rely on its lease and pooling agreement to support its right to use the road on the Hegars' land.<sup>21</sup> In summary, the Hegars acquired a surface estate which was not subject to an existing lease.

However, as a mineral lessee of an interest in the Curbo Tract, "Key Operating has the same surface rights [the mineral owner] has always had: the right to use the surface of the Curbo Tract to produce oil from beneath the surface, regardless of whether that oil is comingled with oil from other tracts."<sup>22</sup> A mineral owner's implied surface "easement necessarily includes the rights of ingress and egress upon the land for the exploration and production of oil and gas."<sup>23</sup> The court held that Key Operating's common law surface easement gave it the right to use the road on the Curbo Tract to produce oil from the Richardson-Curbo Unit so long as part of the purpose for using the road included obtaining production from the Curbo Tract.<sup>24</sup> Thus, while the Hegars were not bound by the terms of Key Operating's lease or pooling agreement, Key Operating had the right to use the road across the Hegars' surface to explore and extract oil from the Curbo Tract, even if the extracted oil was comingled with oil from the Richardson Tract and produced using a well on the Richardson Tract pursuant to a pooling agreement.<sup>25</sup> The opinion is a thorough analysis of the scope of the common law implied easement and the limits imposed by, and the relationship to, the accommodation doctrine.<sup>26</sup>

The court expressly rejected the Hegars' theory that the mineral owners' surface rights were restricted to those that existed at the time of the mineral severance, which would effectively preclude pooling by anyone who did not also own the surface estate, and which would be contrary to Texas public policy.<sup>27</sup> The court held that the right to use the surface of the Curbo Tract to access the Richardson-Curbo Unit wells was supported by "(1) the nature of the implied surface easement, (2) practical and public policy considerations, and (3) analogous cases," but only "so long as that production includes production from

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18. *Id.* at 326.

19. *Id.* (quoting *SWEPI LP v. R.R. Comm'n of Tex.*, 314 S.W.3d 253, 256 (Tex. App.—Austin 2010, pet. denied)).

20. *Id.*

21. *Id.*

22. *Id.* at 325.

23. *Id.* at 326 (citing *Ball v. Dillard*, 602 S.W.2d 521, 523 (Tex. 1980)).

24. *Id.*

25. *Id.* at 325.

26. *Id.* at 329–30.

27. *Id.* at 327.

the Curbo Tract.”<sup>28</sup>

The trial court, after listening to competing experts, determined that no oil was being produced from the Curbo Tract.<sup>29</sup> In the absence of a pooling or similar agreement to which the Hegars consented or to which they or their title are otherwise subject, Key Operating had no right to use the road across the Hegars’ surface for the purpose of producing oil that was being produced only from the Richardson Tract.<sup>30</sup>

The dissenting opinion is based largely on the belief that the majority opinion turns on the accommodation doctrine.<sup>31</sup> However, the majority opinion generally discusses the accommodation doctrine only in the context of being the remedy for the surface owner whose surface use is impaired or limited. This case turned on whether the implied surface easement existed when there was no production from the surface owner’s tract. The majority also noted that the case related exclusively to injunctive relief.<sup>32</sup> The issue was not excessive use or the reasonableness of use, which could subject a mineral owner or lessee to liability for damages.<sup>33</sup>

This case is important because it broadly supports surface uses related to pooling and off-lease unit production and comingling of that production, provided only that there is evidence of some production from the tract subjected to the surface use. The production fact question will be troublesome, because it will generally require expert testimony to obtain a finding. Prior to trial, uncertainty is generally leverage for the surface owner. Presumably, “production” in this context is not limited to actual production, but includes operations intended to obtain production. However, there are many Texas cases holding that “production” means actual production under other facts and circumstances.

*Wynne/Jackson Development, L.P. v. PAC Capital Holdings, Ltd.*<sup>34</sup> held that a conveyance of a non-participating royalty interest (NPRI) was effective to convey a fractional royalty of 1/16 of production.<sup>35</sup> The parties aligned as successors-in-interest to the Grantor and Grantee under three deeds with an identical issue.<sup>36</sup> The deeds reserved to Grantor an NPRI equal to “one-half (1/2) of the usual one-eighth (1/8) royalty in and to all oil, gas, and other minerals produced, saved and sold.”<sup>37</sup> A subsequent lease provided for royalty payments equal to 1/4 of production.<sup>38</sup> The issue in the case was whether Grantor reserved 1/16 of production (1/2 of 1/8 = 1/16 [fractional royalty]) or 1/8 of production (1/2 of 1/4 = 1/8 [fraction of royalty]).<sup>39</sup>

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28. *Id.*

29. *Id.* at 336.

30. *Id.*

31. *Id.* at 336–38 (Sharp, J., dissenting).

32. *Id.* at 331.

33. *Id.*

34. *Wynne/Jackson Development, L.P. v. PAC Capital Holdings, Ltd.*, No. 13-12-00449-CV, 2013 WL 2470898 (Tex. App.—Corpus Christi June 6, 2013, pet. denied).

35. *Id.* at \*1.

36. *Id.*

37. *Id.* at \*4.

38. *Id.* at \*1.

39. *Id.* at \*1–2.

The Texas Supreme Court has construed “one-half of one-eighth of the oil, gas and other mineral royalty” to mean a 1/16 fractional royalty.<sup>40</sup> The language that the Court construed did not contain the words “the usual.”<sup>41</sup> The San Antonio Court of Appeals has construed “an undivided one-fourth of the usual one-eighth royalty in all of the oil, gas or other minerals produced, saved and sold from the premises conveyed under the terms of any valid oil and gas lease” to mean a 1/32 fractional royalty.<sup>42</sup> The court found these precedents to be persuasive and held that the deeds reserved a 1/16 fractional royalty as a matter of law, after relying upon the usual canons of construction: determining the intent of the parties, the “four corners” rule, and harmonizing all parts.<sup>43</sup>

There continues to be some tension between various opinions construing the effect of the words “the usual 1/8 royalty” when used in instruments executed during the time when the lease royalty was almost always 1/8. The tilt seems to be toward holding that the words are merely descriptive of the fractional royalty conveyed or reserved, rather than objective evidence of an intent to create a fraction of royalty (floating royalty).

*Gonyea v. Kerby*<sup>44</sup> construed two conflicting contracts for deed against the draftsman after considering extrinsic evidence. Gonyea contracted with Kerby to sell and convey two lots that together comprised just over two acres in Alvarado, Texas. Gonyea drafted two contracts for deed, signed them, and sent them to Kerby. Kerby signed both, sent one back to Gonyea, and Kerby kept the other. The contract retained by Kerby stated that the mineral rights in the property would be conveyed to the purchaser when the note for the deed had been paid in full, while the contract returned to Gonyea stated just the opposite—that no mineral rights would be conveyed to the purchaser even when the note was paid in full. By the contract’s terms, it was a monthly installment sale over a fifteen-year term.<sup>45</sup> In 2005, Gonyea signed an oil and gas lease on the property.<sup>46</sup> In 2008, shortly before the final payment was due, Kerby noticed that there was oil and gas activity happening on the property and contacted Gonyea to inquire about the mineral rights.<sup>47</sup> Gonyea told Kerby that Kerby did not own the mineral rights and that they were not for sale.<sup>48</sup> Kerby made his final payment, and when Gonyea refused to convey the minerals, Kerby sued Gonyea for breach of contract.<sup>49</sup>

The parties agreed that their agreement was ambiguous, and Kerby obtained a jury verdict on his breach-of-contract claim.<sup>50</sup> The issue on appeal was the

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40. *Id.* at \*4 (quoting *Harris v. Ritter*, 279 S.W.2d 845, 847 (Tex. 1955)).

41. *Id.*

42. *Id.* (quoting *Pickens v. Hope*, 764 S.W.2d 256, 258-59 (Tex. App.—San Antonio 1988, writ denied)).

43. *Id.* at \*5.

44. *Gonyea v. Kerby*, No. 10-12-00182-CV, 2013 WL 4040117 (Tex. App.—Waco Aug. 8, 2013, pet. filed) (mem. op.).

45. *Id.* at \*1.

46. *Id.* at \*1 n.2.

47. *Id.* at \*1.

48. *Id.*

49. *Id.* at \*2.

50. *Id.*

sufficiency of the evidence to support the jury finding that the parties had agreed to convey the minerals.<sup>51</sup>

The court found that neither contract, when read alone, was ambiguous, and that the ambiguity only results from reading the two contracts together.<sup>52</sup> The court cited the usual rules of construction that the intent of the parties is to be determined from the written agreement and that separate instruments executed at the same time, between the same parties, and relating to the same subject matter may be considered together and construed as one contract.<sup>53</sup> The court resolved this conundrum by concluding that the jury had, in effect, picked which contract was the agreement between the parties, and the determination of which contract was the agreement was a fact question. The existence of the second contract that differed from the first was parol evidence indicating that there were issues of fact for the jury to decide. The fact that Gonyea drafted two contracts and Kerby kept one of the contracts was enough for the jury to find that the parties agreed on the contract Kerby kept.<sup>54</sup>

Moreover, if forced to construe the two contracts together, the court held that it would still find for Kerby as a matter of law because Gonyea drafted both of the contracts for deed. Texas law provides that contracts are to be construed against the draftsman.<sup>55</sup>

Because the two contracts were so clearly irreconcilable, the case highlights the significance of a fact finding at the trial court level regarding the “agreement” of the parties, and the risk of being the draftsman under the law applicable to the construction of the agreement of the parties.

### III. LEASE AND LEASING ISSUES<sup>56</sup>

*Stroud Prod., L.L.C. v. Hosford*<sup>57</sup> held that a lessee could intentionally wash out an overriding royalty interest by allowing the burdened lease to terminate while acquiring an unburdened top lease.<sup>58</sup> In 1978, the lessor granted two leases (Base Leases) that were subsequently drilled, produced, and burdened by a combined 5% overriding royalty held by Hosford, et al. (Hosford).<sup>59</sup> In

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51. *Id.*

52. *Id.* at \*5 n.4.

53. *Id.* at \*4.

54. *Id.* at \*5.

55. *Id.*

56. Other notable cases dealing with lease and leasing issues include the following: *Wade v. XTO Energy Inc.*, No. 02-12-00007-CV, 2013 WL 257361 (Tex. App.—Fort Worth Jan. 24, 2013, no pet.) (mem. op.) (lease and statute of frauds); *Bradshaw v. Steadfast Fin., L.L.C.*, 395 S.W.3d 348 (Tex. App.—Fort Worth 2013, pet. filed) (duty owed by executive to NPRI owner); *Potts v. Chesapeake Exploration, L.L.C.*, No. 3:12-CV-1596-O, 2013 WL 874711 (N.D. Tex. Mar. 11, 2013) (mem. op.) (net-back market value at point of sale); *Fain Family First Ltd. P'ship v. EOG Res. Inc.*, No. 02-12-00081-CV, 2013 WL 1668281 (Tex. App.—Fort Worth Apr. 18, 2013, no pet.) (mem. op.) (shut-in royalty on well not connected to pipeline); *Torch Energy Advisors Inc. v. Plains Exploration & Prod. Co.*, 409 S.W.3d 46 (Tex. App.—Houston [1st Dist.] 2013, pet. filed) (recovery of overpaid royalty); *Lucas v. Chesapeake Exploration, L.L.C.*, No. 2:12-CV-00592-JRG, 2013 WL 5200046 (E.D. Tex. Sept. 16, 2013) (class action on deductions of post-production costs).

57. *Stroud Prod., L.L.C. v. Hosford*, 405 S.W.3d 794 (Tex. App.—Houston [1st Dist.] 2013, pet. filed).

58. *Id.*

59. *Id.* at 798.

December 2003, Stroud et al. (Stroud) acquired the Base Leases and assumed operations.<sup>60</sup> In January 2004, production ceased because of a minor mechanical problem.<sup>61</sup> In February 2004, Stroud acquired Top Leases on different terms on the same property.<sup>62</sup> In April 2004, the Base Leases terminated for failure to resume production within the time permitted under the ninety-day continuous operations clause.<sup>63</sup> In May 2004, Stroud fixed the mechanical problem and promptly resumed production, but under the Top Leases.<sup>64</sup> The assignments of overriding royalty to Hosford burdening the Base Leases did not contain renewal and extension clauses.<sup>65</sup> Stroud refused to pay overriding royalty to Hosford.<sup>66</sup> “Stroud admitted that he intentionally returned the well to production in June 2004, only after the [Base Leases] had terminated, [the Top Leases] had been obtained, and the 90-day continuous operations period had passed. He also admitted that he ‘did not want any overriding royalty interest on the new leases and [Hosford’s] overriding royalty interests had been ‘washed out.’”<sup>67</sup> There was no express surrender clause in the Base Leases.<sup>68</sup>

The issue was whether Texas recognizes a cause of action for intentional termination of an overriding royalty interest.<sup>69</sup> The court surveyed in detail relevant Texas cases on the duty a lessee owes to an overriding royalty interest holder under Texas law.<sup>70</sup> The court concluded that:

In sum, no Texas court has yet recognized that a lessee generally owes any type of duty, whether it be an implied contractual covenant or a fiduciary-type duty, to protect the interest of an overriding royalty interest holder so as to require the lessee to make repairs to well equipment, perpetuate the lease, and ensure that such overriding interests are not extinguished.<sup>71</sup>

The court observed that the two Texas Supreme Court opinions on topic, *Sunac Petroleum Corp. v. Parkes*<sup>72</sup> and *Ridge Oil Co. v. Guinn Investments, Inc.*,<sup>73</sup> indicate that although the question of whether any duty is owed is uncertain under Texas law, the language of the controlling documents, and the circumstances and relationships of the parties should be considered when making such a determination.<sup>74</sup>

As to the circumstances and relationship of the parties, the court found no evidence of a formal fiduciary relationship between Stroud and Hosford, and

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60. *Id.* at 799.

61. *Id.*

62. *Id.* at 800.

63. *Id.* at 799.

64. *Id.* at 800.

65. *Id.* at 799.

66. *Id.* at 798–800.

67. *Id.* at 799–800.

68. *Id.* at 810.

69. *Id.* at 797.

70. *Id.* at 803–09.

71. *Id.* at 809.

72. *Sunac Petroleum Corp. v. Parkes*, 416 S.W.2d 798 (Tex. 1967).

73. *Ridge Oil Co. v. Guinn Investments, Inc.*, 148 S.W.3d 143 (Tex. 2004).

74. *Stroud*, 405 S.W.3d at 809.



there was no special relationship of trust and confidence spanning over a long period of time.<sup>75</sup> Thus, there was no relationship duty.

As to the language of the controlling documents, the court first observed that the assignments of overriding royalty did not include a renewal or extension clause, which some courts have suggested may provide some evidence of a fiduciary relationship or support a constructive trust remedy.<sup>76</sup> However, those same courts then noted that when the underlying lease has an express surrender clause, there can be no implied duty to keep the lease in effect.<sup>77</sup> Thus, the court noted that a renewal clause, if it existed, could provide some evidence of a fiduciary relationship, but it would not be determinative.<sup>78</sup> The Base Leases did not include an express surrender clause that would permit the lessee to terminate the leases at will and thereby support the conclusion that there is no duty owed by the lessee to the overriding royalty owner. However, at least one Texas court has held that the absence of an express surrender clause in the lease, even when there is a renewals and extensions clause in the assignment of overriding royalty, is not enough to impose a duty.<sup>79</sup>

Here the court did not find anything in the assignment of the overriding royalty interest or the Base Leases that obligated Stroud to take other action to perpetuate the lease, and therefore, the absence of an express surrender clause in the Base Leases did not indicate some sort of special duty that Stroud owed Hosford.<sup>80</sup> The court concluded that while a party that engages in conduct to intentionally wash out an overriding royalty interest may be subject to liability, because here there was no evidence that Stroud violated any express or implied contractual duty and there was no evidence of the existence of a fiduciary or confidential relationship, Stroud did not commit an actionable wrong by intentionally terminating the Base Leases to extinguish the overriding royalty interest.<sup>81</sup> There is a lengthy dissent that is generally based on the fact that there was no express surrender clause in the Base Leases.<sup>82</sup> It reads the Base Leases into the assignment of overriding royalty interests to conclude that lease clauses, such as the implied covenant to reasonably develop, created duties that the lessee owed to the overriding royalty owner.<sup>83</sup>

This case appears to squarely raise the issue of the duty owed by the lessee to the holder of an overriding royalty interest in a “wash-out” transaction. This case holds that there is no duty owed, in the absence of renewals and extensions clause, if the lessee is simply pursuing its own best interests.

*Cabot Oil & Gas Corp. v. Healey, L.P.*<sup>84</sup> held that an oil and gas lease

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75. *Id.* at 809–10.

76. *Id.* at 810.

77. *Id.*

78. *Id.*

79. *Id.* (citing *Exploration Co. v. Vega Oil & Gas Co.*, 843 S.W.2d 123, 124, 126 (Tex. App.—Houston [14th Dist.] 1992, writ denied)).

80. *Id.*

81. *Id.* at 811 (citing *Keese v. Cont'l Pipe Line Co.*, 235 F.2d 386, 388 (5th Cir. 1956)).

82. *Id.* at 814–35 (Keyes, J., dissenting).

83. *Id.*

84. *Cabot Oil & Gas Corp. v. Healey, L.P.*, No. 12-11-00236-CV, 2013 WL 1282007 (Tex. App.—Tyler Mar. 28, 2013, pet. denied) (mem. op.).

terminated for breach of covenant. Cabot Oil & Gas Corporation (Cabot) was the lessee and operator of three oil and gas leases and Healey, L.P. (Healey) was the lessor. There were multiple production units and at least twenty-one wells were drilled.<sup>85</sup> The leases each contained the following provisions:

Lessee shall, during the drilling of any wells on the leased premises, furnish Lessor daily drilling reports, copies of all logs runs, monthly production reports for the life of said well(s), copies of all reports and forms filed with the State regulatory bodies in connection with such wells, well locations, dates of completion and abandonment. Lessee shall also furnish Lessor copies of any title opinions or title reports which Lessee may obtain on the leased premises.

\* \* \*

Any breach by Lessee of any term, provision[,] or covenant in this lease shall be grounds for cancellation of this lease (together with any other remedies available to Lessor).<sup>86</sup>

Healey alleged that Cabot and Cabot's predecessor had failed to furnish the information as required by the leases, suggested that the leases had terminated, and requested to be treated as a working interest owner in the pooled units. Cabot responded by attempting to provide the missing data. Healey filed suit asserting claims for breach of contract, seeking a declaratory judgment that the leases had terminated and that Healey was an unleased cotenant, and requesting an accounting.<sup>87</sup> That these leases could terminate for breach of covenant was apparently uncontroverted, and the issues in the case were generally procedural and matters of proof.

The case was tried as a declaratory judgment action rather than in trespass to try title.<sup>88</sup> The court reviewed various Texas cases that were illustrative of the difference between the two causes of action, and concluded that, "[w]ith an exception not applicable here, a trespass to try title claim is the exclusive method in Texas for adjudicating disputed claims of title to real property."<sup>89</sup> Because the case should have been in trespass to try title, Cabot contended that the declaratory judgment should be reversed,<sup>90</sup> that attorney's fees could not be awarded,<sup>91</sup> and that Healey had failed to meet the strict evidentiary burdens required in trespass to try title.<sup>92</sup> The court held that Cabot failed to preserve error on all of those points by not submitting an exception in writing to the trial court prior to the submission of the charge under Texas Rule of Civil Procedure 90.<sup>93</sup>

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85. *Id.* at \*1.

86. *Id.*

87. *Id.*

88. *Id.*

89. *Id.* at \*2 (citing TEX. PROP. CODE ANN. § 22.001(a) (West 2000)).

90. *Id.*

91. *Id.* at \*3.

92. *Id.* at \*5.

93. *Id.* at \*3-5.

Much of the proof required to establish drilling costs on each well was dependent upon a business records affidavit with multiple records attached as provided by Cabot's predecessor.<sup>94</sup> Cabot's well-by-well payout methodology was apparently unchallenged, but the underlying evidence was contested on the basis of Healey's objections that the exhibit was hearsay, constituted an impermissible summary, and failed to demonstrate that the costs set forth therein were reasonable and necessary.<sup>95</sup> The trial court sustained Healey's objections and excluded the evidence; however, this decision was reversed on appeal.<sup>96</sup> Of particular note, the court held that evidence that the costs were reasonable and necessary was not required to secure admissibility of the business records, but only as an element of proof of the defense of offset.<sup>97</sup>

Having held that the exhibit was improperly excluded, the court next weighed the gravity of the harm to Cabot as a result of the exclusion. The court recited the rule that an error causes harm if it is dispositive of a material issue.<sup>98</sup> Here, although Cabot was precluded from introducing the exhibit into evidence, it would still have been required to show that the expenses outlined in the exhibit were reasonable and necessary.<sup>99</sup> Surprisingly, after reviewing and analyzing the evidence and the relationship between Cabot and its predecessor, the court held that Cabot did not and could not demonstrate that the costs outlined in the exhibit were reasonable and necessary. Thus, the exclusion of the exhibit was not harmful.<sup>100</sup>

Perhaps Cabot's best chance to preserve its leases on the merits was the affirmative defense of substantial performance, but the trial court refused Cabot's requested issue.<sup>101</sup> The court noted that jury instructions are reviewed under an abuse of discretion standard, and if any part of the question, instruction, or definition fails, then the court can deny the entire request.<sup>102</sup> Instructions should not have the effect of "advis[ing] the jury of the effect of its answers."<sup>103</sup> Here, the proposed instructions would have advised the jury that if they answered in the affirmative, Healey would not be able to terminate the leases.<sup>104</sup> Cabot stretched too far for this court. Accordingly, the court held that the trial court did not err by refusing to submit the proposed question.<sup>105</sup> The trial court's rejection of proposed questions on waiver and quasi-estoppel was also affirmed on appeal.<sup>106</sup>

Finally, the court considered whether the trial court erred by not allowing the recovery of costs from a dry hole that produced data that aided in the

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94. *Id.* at \*5.

95. *Id.*

96. *Id.* at \*5-8.

97. *Id.* at \*8.

98. *Id.* at \*9 (citing *Mentis v. Barnard*, 870 S.W.2d 14, 16 (Tex. 1994)).

99. *Id.*

100. *Id.* at \*10.

101. *Id.* at \*11.

102. *Id.* at \*10.

103. *Id.* at \*11 (citing TEX. R. CIV. P. § 277).

104. *Id.*

105. *Id.*

106. *Id.* at \*12-15.

development of the unit as a whole.<sup>107</sup> The court avoided that issue because, regardless of the benefit to the land, Cabot had produced no evidence that the expenses associated with the dry hole were reasonable and necessary.<sup>108</sup>

The significance of this case is that it confirms conventional wisdom that a lease provision making the lease determinable upon breach of covenant is simply unacceptable to any lessee. How to resolve cases tried as declaratory judgments that should have been tried in trespass to try title is now a common problem. It is perhaps a new approach to hold that the party who happens to lose the trial is stuck on appeal because neither party objected to the failure of both parties to use the exclusive method in Texas for adjudicating disputed claims of title to real property.

*PanAmerican Operating, Inc. v. Maud Smith Estate*<sup>109</sup> held that an independent landman's apparent authority and the company's failure to promptly repudiate an oil and gas lease made the lease binding on the company. PanAmerican Operating, Inc. (PanAm) hired landmen as independent contractors, including Robert Wormser (Wormser).<sup>110</sup> PanAm provided Wormser with a cubicle, an office landline, a company email domain name, and the president of PanAm knew exactly what Wormser was doing on behalf of PanAm.<sup>111</sup> Wormser contacted William Elder (Elder), the attorney responsible for negotiating leases on behalf of the Maud Smith Estate (Maud), to negotiate a lease on Maud's property for PanAm.<sup>112</sup> Wormser identified himself as a PanAm representative but never disclosed that he was an independent contractor.<sup>113</sup> Wormser and Elder agreed on terms, and Wormser sent Elder a form lease from his PanAm email account.<sup>114</sup> On June 2, 2008, Elder accepted and emailed a copy of the signed lease to Wormser and asked for the lease bonus.<sup>115</sup> On July 21, 2008, Elder sent the original lease to PanAm.<sup>116</sup> On August 12, 2008, PanAm acknowledged receipt of the lease.<sup>117</sup> After the price of oil dropped precipitously, PanAm asserted that Wormser had no authority to execute leases on its behalf.<sup>118</sup> Apparently, PanAm dodged the payment questions from Elder for about three months before repudiating the validity of the lease, and PanAm's possession of the lease prevented Maud from leasing to a third party.<sup>119</sup> Maud sued PanAm for breach of contract based on failure to pay the lease bonus.<sup>120</sup> The issues on appeal were whether Wormser held the apparent authority to bind PanAm and whether PanAm ratified the lease by failing to timely repudiate

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107. *Id.* at \*15.

108. *Id.* at \*17.

109. *PanAmerican Operating, Inc. v. Maud Smith Estate*, 409 S.W.3d 168 (Tex. App.—El Paso 2013, pet. denied).

110. *Id.* at 171.

111. *Id.* at 173–74.

112. *Id.* at 171.

113. *Id.*

114. *Id.*

115. *Id.* at 171, 178 n.4.

116. *Id.*

117. *Id.* at 178 n.4.

118. *Id.* at 174–75.

119. *Id.* at 178 n.4.

120. *Id.* at 171.

the lease.<sup>121</sup>

“Apparent authority arises when a principal either knowingly permits its agent to hold himself out as having authority or acts with such a lack of ordinary care as to clothe its agent with indicia of authority.”<sup>122</sup> Silence may also constitute a manifestation of apparent authority.<sup>123</sup> It was undisputed that Wormser had authority to obtain leases on PanAm’s behalf and to negotiate on PanAm’s behalf.<sup>124</sup> The court held that a reasonably prudent person would have believed Wormser possessed the authority to contract on PanAm’s behalf because PanAm acted with “such a lack of ordinary care as to clothe Wormser with indicia of authority.”<sup>125</sup>

“Ratification is the adoption or confirmation, by a party with actual knowledge of all material facts, of a prior act that did not then legally bind that party and which that party had a right to repudiate.”<sup>126</sup> “A party ratifies a contract by acting under it, performing under it, or affirmatively acknowledging it.”<sup>127</sup> PanAm knew all the material facts surrounding Wormser’s acquisition of the lease, and “by keeping the lease and failing to repudiate it when presented with the opportunity to do so, [PanAm] affirmatively acknowledged its validity, thereby ratifying it.”<sup>128</sup>

PanAm argued there was no clear evidence PanAm intended to ratify the lease.<sup>129</sup> The court dismissed this argument because Maud was only required to demonstrate that PanAm performed an “intentional act that was inconsistent with any intention to avoid the lease.”<sup>130</sup> The “intent may be inferred from the acceptance of benefits under the lease after having full knowledge of the act that would make the lease voidable.”<sup>131</sup> The benefit PanAm received was obtaining a signed lease without having to pay until PanAm determined whether honoring the lease made economic sense.<sup>132</sup> Therefore, PanAm ratified the lease by failing to repudiate after obtaining sufficient knowledge of the facts.<sup>133</sup>

The significance of this case is that it highlights the risk in failing to promptly repudiate a lease or a contract to lease. The industry frequently uses contract landmen, and the facts in this case were particularly bad for PanAm. But the issues about authority can arise in a narrower context, such as the specific business points (bonus, royalty, term) in a lease, other lease provisions, or the lease form itself. Such issues would be more common than a complete

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121. *Id.* at 176.

122. *Id.* at 172 (citing *Gaines v. Kelly*, 235 S.W.3d 179, 182 (Tex. 2007)).

123. *Id.* at 172-73 (citing Restatement (Third) of Agency § 1.03, cmt. b (2006)).

124. *Id.* at 173.

125. *Id.*

126. *Id.* at 176 (citing *Thomson Oil Royalty, LLC v. Graham*, 351 S.W.3d 162, 165 (Tex. App.—Tyler 2011, no pet.)).

127. *Id.* (citing *Thomson Oil*, 351 S.W.3d at 166).

128. *Id.* at 177.

129. *Id.*

130. *Id.* (citing *Old Republic Ins. Co., Inc. v. Fuller*, 919 S.W.2d 726, 728 n.1 (Tex. App.—Texarkana 1996, writ denied)).

131. *Id.* (citing *Williams v. City of Midland*, 932 S.W.2d 679, 685 (Tex. App.—El Paso 1996, no pet.)).

132. *Id.*

133. *Id.*

repudiation of authority, but the landman's apparent authority and the company's acquiescence will be equally important on those issues.

#### IV. INDUSTRY CONTRACTS<sup>134</sup>

*Indian Oil Company, LLC v. Bishop Petroleum Inc.*<sup>135</sup> held that in the absence of an express or implied release, a non-operator assigning its interest under a 1989 M.F.O.A. remains liable for operating costs and plugging and abandonment costs. Bishop Petroleum (Operator) was the operator under an A.A.P.L. Form 610–1989 Joint Operating Agreement (JOA) for a well in Escambia County, Alabama. Operator drilled the Scott Paper 27-1 Well, which produced from 1993 until 2007. William E. Trotter, II (Non-Operator) was a non-operating working interest owner under the JOA. In 2002, Non-Operator assigned his 8.5% working interest in the well to Indian Oil Company, LLC (Assignee), notified Operator of the assignment, and thereafter, Operator distributed revenues and billed expenses to Assignee.<sup>136</sup>

When the well stopped producing in 2007, Operator eventually proposed a workover under the “July AFE” in the amount of \$589,800, which Assignee and various other working interest owners approved, but it was not approved by Non-Operator. Workover operations started on October 1, 2007, and were more difficult and lengthy than Operator anticipated. As a result, Operator abandoned the workover efforts in January 2008 after incurring approximately \$1.6 million in costs. In 2009, Operator sent an AFE to the working interest owners in the amount of \$243,300 for plugging and abandonment.<sup>137</sup>

Neither Operator nor Assignee paid any expenses associated with the reworking or plugging and abandonment.<sup>138</sup> Operator sued Non-Operator, Assignee, and various other working interest owners for breach of contract, quantum meruit, and unjust enrichment.<sup>139</sup> Operator prevailed in the trial court, and only Non-Operator appealed.<sup>140</sup>

Non-Operator contended that Operator had breached the JOA as a matter of law by (1) failing to provide daily workover reports<sup>141</sup> and (2) failing to issue a new AFE when the workover became dramatically more complex and expensive than the original AFE anticipated.<sup>142</sup> Non-Operator also contended that its

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134. Other notable cases dealing with industry contracts include the following: *El Paso Field Services, L.P. v. MasTec North America, Inc.*, 389 S.W.3d 802 (Tex. 2012) (pipelines and undiscovered foreign crossings); *Lillis v. Kachina Pipeline Co., Inc.*, No. 03-10-00784-CV, 2013 WL 3186261 (Tex. App.—Austin June 18, 2013, pet. filed) (mem. op.) (gas gathering agreement); *Lamont v. Vaquillas Energy Lopeno Ltd., LLP*, 421 S.W.3d 198 (Tex. App.—San Antonio 2013, pet. filed) (misappropriation of seismic maps as trade secret); *Eagle Oil & Gas Co. v. TRO-X, L.P.*, No. 11-11-00290-CV, 2013 WL 5861496 (Tex. App.—Eastland Oct. 31, 2013, no pet.) (construction of participation agreement).

135. *Indian Oil Company, LLC v. Bishop Petroleum Inc.*, 406 S.W.3d 644 (Tex. App.—Houston [14th Dist.] 2013, pet. filed).

136. *Id.* at 647.

137. *Id.* at 648.

138. *Id.*

139. *Id.* at 648–49.

140. *Id.* at 649.

141. *Id.* at 653–54.

142. *Id.* at 654–55.

liability for costs incurred should be limited to costs incurred in connection with operations in which Non-Operator agreed to participate prior to Non-Operator's assignment to Assignee.<sup>143</sup>

Non-Operator's argument as to daily workover reports was based on Article V.D.7(b) of the JOA, which stated, "Operator will send to Non-Operators such reports, test results, and notices regarding the progress of operations on the well as the Non-Operators shall reasonably request, including, but not limited to, daily drilling reports, completion reports, and well logs."<sup>144</sup> The court noted that this language requires the operator to provide such reports as non-operators "reasonably request," and did not require the provision of "any and all requested reports."<sup>145</sup> Because Non-Operator never requested a report, Operator's failure to provide reports could not be considered breach of contract.<sup>146</sup> Non-Operator also alleged that Operator was under a duty to provide daily workover reports because such reports had been requested by one of the other working interest owners.<sup>147</sup> The court noted that Non-Operator offered no authority for the proposition that "one working interest owner's request for reports obligated [Operator] to send reports to every working interest owner, including those who made no such request."<sup>148</sup> The court held that Non-Operator did not establish that by failing to provide workover reports, Operator had breached the JOA as a matter of law.<sup>149</sup>

Non-Operator also contended that Operator should have issued a new AFE when the workover operations contemplated by the July AFE became dramatically more expensive than originally anticipated and additional operations were undertaken, and that Operator's failure to do so was a breach of the JOA. Non-Operator contended that the evidence established Operator's breach as a matter of law, but the court noted that the evidence was contradictory. An expert witness had testified that issuing a new AFE would have required dismissing the workover rig and that the fishing operations that were conducted were a normal part of the kinds of workover operations contemplated by the July AFE. Therefore, the court held that Non-Operator had failed to show that Operator had breached the JOA.<sup>150</sup>

The jury found that Non-Operator was liable for \$336,393.42 for expenses incurred under the JOA. Non-Operator argued that there was no evidence to support this amount because (1) Non-Operator had assigned his interest to Assignee in 2002, and Non-Operator was thus not liable for expenses subsequently incurred under the JOA, and (2) Non-Operator had not consented to the July AFE, and therefore, could not have incurred any expenses under it.<sup>151</sup>

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143. *Id.* at 655-66.

144. *Id.* at 654.

145. *Id.*

146. *Id.*

147. *Id.*

148. *Id.*

149. *Id.* at 655.

150. *Id.* at 654-55.

151. *Id.* at 656.

The parties' disagreement on this issue centered on different interpretations of the Texas Supreme Court's opinion in *Seagull Energy E & P, Inc. v. Eland Energy, Inc.*<sup>152</sup> The Supreme Court held that an assignor of a working interest subject to a joint operating agreement remained liable for operating expenses when the assignee failed to pay for the operating expenses attributable to that interest (in *Eland*, plugging and abandonment costs).<sup>153</sup> Operator asserted that, under *Eland*, in the absence of an express or implied release, Non-Operator remained liable for *all* expenses incurred under the JOA, notwithstanding Operator's assignment to Assignee.<sup>154</sup> This court distinguished *Eland*, because the operating agreement construed in *Eland* did not address the assignor's liability for expenses incurred subsequent to the assignment. It was silent as to continuing liabilities.<sup>155</sup> The JOA in this case was not silent as to a party's ongoing liability subsequent to an assignment.<sup>156</sup> The pertinent language from the JOA provided:

[N]o assignment or other disposition of interest by a party shall relieve such party of obligations previously incurred by such party hereunder with respect to the interest transferred, including without limitation the obligation of a party to pay all the costs attributable to an operation conducted hereunder in which such party has agreed to participate prior to making such assignments.<sup>157</sup>

This language made Non-Operator liable for expenses "previously incurred," i.e., incurred before Non-Operator assigned to Assignee.<sup>158</sup> Non-Operator conceded that Non-Operator continued to be liable for monthly operating costs and the costs of plugging and abandoning the well.<sup>159</sup> However, Non-Operator had assigned the working interest to Assignee in 2002, and Operator did not request approval for the workover until 2007.<sup>160</sup> Under the "previously incurred" language, Non-Operator could not be liable for expenses incurred pursuant to the July AFE.<sup>161</sup>

The amount the jury awarded included workover costs, monthly operating expenses, and plugging and abandonment expenses.<sup>162</sup> Although the evidence was insufficient to support the entire damage amount awarded against Non-Operator, it was sufficient to support some damages.<sup>163</sup> The court remanded the case to determine liability and damages.<sup>164</sup>

The significance of the case is that it limits the continuing obligations of non-

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152. 207 S.W.3d 342 (Tex. 2006).

153. *Indian Oil Co.*, 406 S.W.3d at 657 (citing *Eland*, 207 S.W.3d at 344).

154. *Id.* at 656.

155. *Id.* at 657–58 (citing *Eland*, 207 S.W.3d at 346–47).

156. *Id.* at 657.

157. *Id.*

158. *Id.* at 658.

159. *Id.*

160. *Id.*

161. *Id.* at 657–58.

162. *Id.* at 659.

163. *Id.*

164. *Id.* at 660.



operators under *Eland*, at least under the 1989 M.F.O.A., to those obligations “previously incurred.” This does not mean accrued, but incurred, so the assigning non-operator will continue to be liable for monthly operating costs, plugging and abandonment costs, and other liabilities included in the operating agreement. Presumably the assigning non-operator will be able to avoid only those subsequent liabilities that require an express subsequent consent. Although the issues on providing reports under an operating agreement generally went off on evidence points, the opinion suggests that under the 1989 M.F.O.A., the obligation to deliver reports requires a reasonable request and not every operational event of a workover will trigger an obligation to issue a new AFE.

*Southwestern Energy Production Co. v. Berry-Helfand*<sup>165</sup> held that the use for personal gain of a prospect analysis disclosed under a confidentiality agreement was a misappropriation of a trade secret. Over the course of several years, Helfand (a reservoir engineer) and her geologist partners conducted a detailed analysis of public and semi-public production data for 600 wells in a six county area.<sup>166</sup> They identified ten sweet spots favorable for production from the James Lime formation with several stacked pays.<sup>167</sup> Helfand focused on two of the prospects where leases were available and began leasing with the object of selling her prospects for cash and an overriding royalty interest.<sup>168</sup> In February 2005, Southwestern Energy Production Company (Sepco) signed a confidentiality agreement with Helfand regarding the materials to be presented by Helfand, and Exhibit A, describing the area subject to the noncompetition agreement, was limited to those two prospects.<sup>169</sup> Helfand then presented to Sepco the results of her research and analysis identifying all ten of the sweet spots.<sup>170</sup> Prior to the presentation, Sepco had no interest in the James Lime because of poor production history.<sup>171</sup> After the presentation, Sepco declined to participate in Helfand’s prospects, because the prospects failed Sepco’s economic criteria.<sup>172</sup> Helfand promptly sold the same two prospects to Petrohawk.<sup>173</sup> Soon after the Helfand/Sepco meeting, Sepco began leasing land in the area of Helfand’s sweet spots, ultimately acquiring 1,800 leases on or near the sweet spots.<sup>174</sup> Two years after the presentation, Sepco drilled a successful James Lime well and then began a large scale drilling program in the James Lime.<sup>175</sup> Ultimately, Sepco drilled or participated in over eighty James Lime wells, all successful and all clustered in and around Helfand’s sweet spots.<sup>176</sup> Helfand filed suit against

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165. *Southwestern Energy Production Co. v. Berry-Helfand*, 411 S.W.3d 581 (Tex. App.—Tyler 2013, pet. filed).

166. *Id.* at 597.

167. *Id.* 597–98.

168. *Id.* at 587.

169. *Id.* at 588.

170. *Id.* at 603.

171. *Id.* at 599.

172. *Id.* at 595.

173. *Id.* at 603.

174. *Id.* at 599.

175. *Id.*

176. *Id.* at 586–89, 600.

Sepco in February 2009.<sup>177</sup> The jury found against Sepco on five liability theories, including common law trade secret misappropriation.<sup>178</sup> The trial court awarded approximately \$11 million in actual damages to Helfand.<sup>179</sup>

“A trade secret is ‘any formula, pattern, device or compilation of information which is used in one’s business and presents an opportunity to obtain an advantage over competitors who do not know or use it.’”<sup>180</sup> The court quickly concluded that Helfand’s “massive compilation and analysis” of data drawn from public and semi-public sources was a trade secret, because it led her to identify sweet spots and stacked pays.<sup>181</sup> Further, the court determined that Helfand’s trade secret was not lost when she shared the material with other operators because these disclosures were conditioned on the execution of confidentiality agreements.<sup>182</sup>

A plaintiff seeking to prevail on a trade secret misappropriation in Texas must prove “(1) the existence of a trade secret, (2) a breach of a confidential relationship or improper discovery of the trade secret, (3) use of the trade secret, and (4) damages.”<sup>183</sup> “Trade secret misappropriation may be proven by circumstantial evidence.”<sup>184</sup> “A person must bring suit for misappropriation of a trade secret no later than three years after the misappropriation is discovered or by the exercise of reasonable diligence should have been discovered.”<sup>185</sup>

Sepco maintained that, even if Helfand’s analysis was a trade secret, there was insufficient evidence to show that Sepco misappropriated the trade secret by unauthorized use.<sup>186</sup> Essentially, Sepco claimed that the circumstantial evidence supporting Helfand’s misappropriation claim amounted to an unsupported “before and after argument,” i.e., Sepco had no James Lime wells before meeting with Helfand and three years later it had more than eighty wells.<sup>187</sup> Sepco also offered other plausible explanations for its James Lime development, claiming that the well locations chosen were the product of its own in-house study.<sup>188</sup>

The court disagreed. Although Sepco had no interest in the James Lime prior to the meeting, in the year that followed, it took approximately 1,800 leases that included James Lime drilling rights, almost all of which were in Helfand’s sweet spots.<sup>189</sup> Thereafter, Sepco drilled more than eighty successful James Lime wells, all of which were in or near Helfand’s sweet spots.<sup>190</sup> The timing of Sepco’s drilling of the James Lime wells coincided with the time required to implement

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177. *Id.* at 589, 602.

178. *Id.* at 590.

179. *Id.*

180. *Id.* at 597 (quoting *In re Bass*, 113 S.W.3d 735, 739 (Tex. 2003)).

181. *Id.* at 597–98.

182. *Id.* at 598.

183. *Id.*

184. *Id.*

185. *Id.* at 602 (citing TEX. CIV. PRAC. & REM. CODE ANN. § 16.010(a) (West 2002)).

186. *Id.* at 598.

187. *Id.* at 599–600.

188. *Id.* at 599.

189. *Id.* at 599–500.

190. *Id.* at 600.

a drilling program to exploit Helfrand's secrets.<sup>191</sup> Further, Sepco failed to produce sufficient independent research to explain its selection of drill sites.<sup>192</sup> According to the court, the circumstantial evidence supporting Helfand's claim was both legally and factually sufficient to support a finding that Sepco misappropriated and used Helfand's trade secrets during the term of the confidentiality agreement.<sup>193</sup>

Sepco also argued that Helfand's claim of misappropriation was barred by the statute of limitations.<sup>194</sup> Sepco maintained that Helfand knew or should have known of her wrongful injury before February 17, 2006, three years before she sued Sepco.<sup>195</sup> In particular, Sepco cited emails Helfand sent in May 2005 that expressed her frustration with Sepco's failure to return all the materials provided at the February 2005 presentation, as well as concern about the possible misuse of her trade secret.<sup>196</sup> Sepco returned her materials shortly thereafter with assurances it retained nothing. Helfand was entitled to rely on these assurances and "had no objective reasonable basis for further inquiry into Sepco's conduct."<sup>197</sup> Even if she had made further inquiries before October 2007, when Sepco drilled its first James Lime well, her investigation would have revealed nothing, because the pattern of James Lime wells would not be apparent for many months thereafter.<sup>198</sup> Helfand testified that she first learned of Sepco's misappropriation in January 2009.<sup>199</sup> Accordingly, the court held that there was no evidence that Helfand knew or should have known that Sepco had misappropriated her trade secret before February 16, 2006.<sup>200</sup>

Several other interesting issues were raised in the case. The court held that confidentiality agreements do not necessarily create fiduciary relationships, and this confidentiality agreement did not create a fiduciary relationship.<sup>201</sup> There can be no theft of a trade secret when the secret is voluntarily delivered.<sup>202</sup> There is an extensive analysis of the appropriate measure of damages, methodology of calculating damages, and proof of damages.<sup>203</sup>

This case is significant because of the holding that a prospect analysis can be a trade secret and that misappropriation may result in substantial liability. Confidentiality agreements are commonly used in the industry; the specific terms and conditions of this confidentiality agreement are commonly included, and the attendant risks and protections are highlighted by this case. Sepco protected itself against the noncompetition provision by limiting the scope of the lands described in Exhibit A, but lost this case because it (1) used the trade

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191. *Id.*

192. *Id.*

193. *Id.*

194. *Id.* at 602.

195. *Id.* at 602-03.

196. *Id.* at 603.

197. *Id.*

198. *Id.* at 603-04.

199. *Id.*

200. *Id.* at 604.

201. *Id.* at 593-94.

202. *Id.* at 599-601.

203. *See id.* at 608-14.

secret, and (2) the use was during the term of the agreement.

*Anadarko Petroleum Corp. v. Williams Alaska Petroleum, Inc.*<sup>204</sup> held that course of performance by the parties was part of a contract for the purchase and sale of oil under the U.C.C. and should be considered regardless of whether the contract was ambiguous. Anadarko sold oil to Williams under two purchase agreements in 2000 and 2002.<sup>205</sup> Both of these agreements contained a provision that tied the contract price for crude oil to other factors, including a third-party accounting arrangement for quality adjustments by the TAPS Quality Bank for oil shipped through the pipeline.<sup>206</sup> The contract price between Anadarko and Williams would be adjusted on a monthly basis according to the anticipated adjustment by Quality Bank, but the actual adjustment would not be known until Williams actually received debits or credits from Quality Bank the following month.<sup>207</sup> The parties would then “true-up” the price, or bring it to the correct balance, in the following month’s invoice based on the actual Quality Bank credits or debits as received by Williams.<sup>208</sup> Several years after the contracts terminated, the Federal Energy Regulatory Commission (FERC) revised the methodology used to assess the quality of oil entering a pipeline and retroactively applied the change, effective as of February 1, 2000.<sup>209</sup> The change in methodology resulted in over a \$9 million credit paid to Williams attributable to Anadarko’s oil.<sup>210</sup> In August 2007, Williams received the credit and refused to pay Anadarko.<sup>211</sup>

The court held that under the U.C.C., “a contract for the sale of oil is a contract for the sale of goods.”<sup>212</sup> Williams contended that, under the U.C.C., the court could not consider evidence of course of performance without first finding that the contracts were ambiguous.<sup>213</sup> The court disagreed and held that “[u]nless carefully negated,” the course of performance becomes “an element of the meaning of the words used,” and that “the course of actual performance by the parties is considered the best indication of what they intended the writing to mean.”<sup>214</sup>

The contract payment provision required that the payments from Williams to Anadarko must be timely, but there was no time limitation on Williams’s obligation to correct any errors in an adjustment found later.<sup>215</sup> In fact, under the parties’ course of performance, adjustments were constantly made to the amount of payment due after the contract payment date had passed to “true up”

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204. *Anadarko Petroleum Corp. v. Williams Alaska Petroleum, Inc.*, 737 F.3 966 (5th Cir. 2013).

205. *Id.* at 968.

206. *Id.* at 968–69.

207. *Id.* at 969.

208. *Id.*

209. *Id.*

210. *Id.* at 969.

211. *Id.* at 971.

212. *Id.* at 969 (citing TEX. BUS. & COM. CODE ANN. § 2.107(a) (West 2009)).

213. *Id.* at 970 (citing TEX. BUS. & COM. CODE ANN. § 2.202, cmt. 1 (West 2009)).

214. *Id.* (quoting TEX. BUS. & COM. CODE ANN. § 2.202, cmt. 2 (West 2009)).

215. *Id.* at 970–71.

the amount due after the receipt of the adjustments from Quality Bank.<sup>216</sup> The court held that, although the FERC's methodology changes did not occur during the contract period, the parties had a history of not treating the payment provision's monthly schedule as conclusive on the obligation to pay a final, correct purchase price.<sup>217</sup>

The court also held that Williams' obligation to pay the correct contract price survived the termination of the contracts.<sup>218</sup> Upon termination of a contract, all executory obligations are discharged, but "any right based on prior breach or performance survives."<sup>219</sup> An obligation is executory if both parties have an obligation yet to be performed.<sup>220</sup> The court held that Williams' obligation to "remit Quality Bank credits . . . is tied to Anadarko's prior tender of the crude oil."<sup>221</sup> Therefore, the court concluded that "where Anadarko has already discharged its full performance under the contract by tendering the oil, Williams Alaska's obligation to pay the correct contract price, including the Quality Bank credits, is no longer executory and thus survives the contract's termination."<sup>222</sup>

Williams also contended that Anadarko's claim was barred by the four-year statute of limitations. The court disagreed and held that the contracts were breached at the time Williams received the adjustments and failed to remit them to Anadarko, which was in August 2007. Anadarko filed suit in March 2011, which was within the limitations period.<sup>223</sup>

The significance of this case is that in contracts governed by the U.C.C. (here, the sale of oil), course of performance is made part of the contract, is admissible without a prior finding of ambiguity, and is considered the best indication of what the parties intended by their agreement. This can only be avoided if carefully negated in the written agreement. Only executory obligations are discharged by contract termination.

## V. LITIGATION ISSUES<sup>224</sup>

*Richmond v. Wells*<sup>225</sup> held that the rights to ownership of the non-possessory

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216. *Id.* at 971.

217. *Id.*

218. *Id.*

219. *Id.* (quoting TEX. BUS. & COM. CODE ANN. § 2.106(c) (West 2009)).

220. *Id.* (quoting *Lee v. Cherry*, 812 S.W.2d 361, 363 (Tex. App.—Houston [14th Dist.] 1991, writ denied)).

221. *Id.*

222. *Id.*

223. *Id.*

224. Other notable cases dealing with litigation issues include the following: *Cabot Oil & Gas Corp. v. Healey, L.P.*, No. 12-11-00236-CV, 2013 WL 1282007 (Tex. App.—Tyler Mar. 28, 2013, pet. denied) (mem. op.) (termination of lease for breach of covenant, failure to object to trial as a declaratory judgment action rather than in trespass to the title, evidence, and submission issues in unleased cotenant cases); *Kadane Corp. v. Cholla Petroleum, Inc.*, No. 11-11-00236-CV, 2013 WL 3336612 (Tex. App.—Eastland June 27, 2013, no pet.) (mem. op.) (disconnection of wells to pipeline as trespass); *Lucas v. Chesapeake Exploration, L.L.C.*, No. 2:12-CV-00592-JRG, 2013 WL 5200046 (E.D. Tex. Sept. 16, 2013) (class action on deduction of post-production costs); *Transocean Offshore Deepwater Drilling, Inc. v. ENI U.S. Operating Co., Inc.*, No. CIV.A. H-12-1366, 2013 WL 5913245 (S.D. Tex. Oct. 1, 2013) (admiralty law governs offshore lease of vessel).

225. *Richmond v. Wells*, 395 S.W.3d 262 (Tex. App.—Eastland 2012, pet. denied).

interests of a lessor under an oil and gas lease (royalty and the possibility of reverter) should be determined in a declaratory judgment action rather than in trespass to try title. Simplified, Richmond owned the minerals in a tract that Richmond leased to Endeavor under a typical oil and gas lease. Endeavor completed and placed the Richmond No. 43 into production on the leased tract.<sup>226</sup> Richmond contracted with Zugg to sell the tract to Zugg, but Richmond would keep his mineral rights.<sup>227</sup> The Richmond-to-Zugg warranty deed was made subject to oil and gas leases of record and excepted “all oil, gas and other minerals in, on or under said land reserved by prior grantors.”<sup>228</sup> Zugg sold to Wells, and the Zugg-to-Wells warranty deed contained the same language.<sup>229</sup> Endeavor suspended royalty payments to Richmond when Wells notified Endeavor that royalty payments should be made to Wells.<sup>230</sup> Richmond and Wells filed competing motions for summary judgment.<sup>231</sup>

Wells’ motion was for declaratory relief under Chapter 37 of the Texas Civil Practice and Remedies code.<sup>232</sup> The trial court granted the motion, holding that both deeds conveyed the mineral estate, that Richmond reserved no interest in the mineral estate, that Richmond was not entitled to any proceeds from the mineral estate, and that Richmond was not entitled to a reformation of the Richmond-to-Zugg deed.<sup>233</sup>

Richmond contended that Wells should have brought his claim in trespass to try title under Chapter 22 of the Texas Property Code and that Wells failed to meet his burden under that cause of action.<sup>234</sup> Richmond relied on *Martin v. Amerman*<sup>235</sup> in which the Texas Supreme Court held generally that trespass to try title is the method for determining title to real property.<sup>236</sup> The court distinguished *Martin* because the facts in that case involved a possessory interest.<sup>237</sup> Under the lease to Endeavor, the lessor retained only a royalty interest and a possibility of reverter, which are non-possessory interests.<sup>238</sup> Claims to a royalty interest and the possibility of reverter are not properly the subject of a trespass-to-try title cause of action.<sup>239</sup> Even though the construction of the two deeds could ultimately impact title and possessory rights to the interests involved, the court held that the legislature did not intend for the trespass-to-try title statute to displace the declaratory judgment statute in this

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226. *Id.*

227. *Id.*

228. *Id.* at 266.

229. *Id.*

230. *Id.*

231. *Id.* at 265.

232. *Id.*

233. *Id.*

234. *Id.* at 266.

235. 133 S.W.3d 262 (Tex. 2004).

236. *Id.* at 262, 267; *Richmond*, 395 S.W.3d at 267.

237. *Richmond*, 395 S.W.3d at 267.

238. *Id.*

239. *Id.* (citing *T-Vestco Litt-Vada v. Lu-cal One Oil Co.*, 651 S.W.2d 284, 289-90 (Tex. App.—Austin 1983, writ ref’d n.r.e.); *Shell Petroleum Corp. v. State*, 86 S.W.2d 245, 249 (Tex. Civ. App.—Austin 1935, no writ)).

case.<sup>240</sup> The declaratory judgment statute expressly provides that any person interested under a deed may have determined any question of construction arising under the deed and obtain a declaration of rights.<sup>241</sup>

Richmond's motion for summary judgment for reformation of the Richmond-to-Zugg deed presumably would have been granted as to Zugg, but the issue in the case was whether Wells was a bona fide purchaser for value without notice of Richmond's claim. Reformation is a claim for equitable relief that will not be granted if there is a bona fide purchaser. The issue was notice.<sup>242</sup>

Richmond argued that Wells had constructive notice based on the pump jack and batteries on the tract. The court held that this would be notice of Endeavor's rights of possession and Endeavor's fee simple determinable ownership interest. "At the time of the Zugg-to-Wells deed, the interests claimed by [Richmond] were non-possessory ones, and Endeavor's possession did not put [Wells] on notice of any interest claimed by [Richmond]."<sup>243</sup> However, there was some evidence that Wells had actual knowledge of Richmond's interest, there were genuine issues of material fact on whether Wells had actual knowledge, and the burden of proof was on Richmond.<sup>244</sup> The court reversed the trial court's judgment granting Wells's motion for summary judgment and remanded for trial.<sup>245</sup>

The opinion appears to hold that the non-possessory interests of a lessor under an oil and gas lease cannot be determined in trespass to try title and must be resolved in a declaratory judgment action. This is probably too broad, but the petition was denied in this case. It is also interesting that the oil and gas operations on the property were apparently held to be insufficient to give constructive notice of the rights of any party, except as to the interests of the lessee conducting the operations.

## VI. REGULATION ISSUES<sup>246</sup>

*In re Texas Rice Land Partners, Ltd.*<sup>247</sup> held that the trial court must make a preliminary finding as to a developer's status as a common carrier before issuing a writ of possession pending final resolution of the landowner's challenge to the developer's common carrier status. Unsuccessful at negotiating the purchase of an easement necessary for its crude petroleum pipeline, TransCanada Keystone Pipeline, L.P. (TransCanada) filed a petition for condemnation of land owned

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240. *Id.*

241. *Id.* (citing TEX. CIV. PRAC. & REM. CODE ANN. § 37.004(a) (West 2008)).

242. *Id.* at 268.

243. *Id.*

244. *Id.* at 268-69.

245. *Id.* at 269.

246. Other notable cases dealing with regulation issues include the following: *Crosstex NGL Pipeline, L.P. v. Reins Rd. Farms-1, Ltd.*, 404 S.W.3d 754 (Tex. App.—Beaumont 2013, no pet.) (pipeline as common carrier); *Crawford Family Farm P'ship v. TransCanada Keystone Pipeline, L.P.*, 409 S.W.3d 908 (Tex. App.—Texarkana 2013, pet. filed) (pipeline as common carrier); *Walton v. City of Midland*, 409 S.W.3d 926 (Tex. App.—Eastland 2013, pet. denied) (city drilling permit and governmental immunity).

247. *In re Texas Rice Land Partners, Ltd.*, 402 S.W.3d 334, 340 (Tex. App.—Beaumont 2013, mandamus denied).

by Texas Rice Land Partners, L.P., James Holland, and David Holland (collectively, TRL). The trial court appointed special commissioners to hear the matter, who then granted TransCanada the easement and awarded TRL \$20,808 in compensation for the easement. TRL objected to the commissioners' decision and requested a jury trial on TransCanada's common carrier status under the Texas Natural Resource Code.<sup>248</sup>

TransCanada filed a motion for a writ of possession pending resolution of the jury trial and deposited the full award of \$20,808 in the court registry, along with a surety bond and cost bond.<sup>249</sup> The court issued the writ of possession to TransCanada, and TRL filed a petition for writ of mandamus, claiming the trial court abused its discretion in granting TransCanada's writ of possession prior to resolving its challenge to TransCanada's common carrier status.<sup>250</sup>

Relying on *Texas Rice Land Partners, Limited v. Denbury Green Pipeline—Texas, LLC*,<sup>251</sup> TRL argued that the trial court was required to fully resolve TransCanada's common carrier status before TransCanada could take possession of TRL's private property in conjunction with its suit for condemnation.<sup>252</sup> In *Denbury Green*, the Texas Supreme Court explained that once a landowner challenges an entity's prima facie evidence of common carrier status pursuant to a permit granted by the Texas Railroad Commission, "the burden falls upon the pipeline company to establish its common-carrier bona fides if it wishes to exercise the power of eminent domain. . . . Merely holding oneself out [as a common carrier] is insufficient under Texas law to thwart judicial review."<sup>253</sup>

However, the court noted that the Supreme Court, in *Denbury Green*, expressly limited its opinion to determining common carrier status under Section 111.002(6) of the Texas Resource Code.<sup>254</sup> The Supreme Court did not address Section 21.021 of the Texas Property Code, the statute at issue in this case.

Section 21.021 allows a party with eminent domain authority to take possession of the condemned property, "pending the results of further litigation" if that party pays the property owner the amount of damages and costs awarded by the special commissioners or deposits the amount of the award into the registry of the court.<sup>255</sup>

"Nevertheless, we recognize that there must be evidence in the record that reasonably supports TransCanada's assertion that it is an entity with 'eminent domain authority,' and it was error for the trial court to refrain from making such a preliminary finding."<sup>256</sup> However, the court held that the trial court's

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248. *Id.* at 336.

249. *Id.*

250. *Id.* at 336–38.

251. *Tex. Rice Land Partners, Limited v. Denbury Green Pipeline—Texas, LLC*, 363 S.W.3d 192 (Tex. 2012).

252. *In re Tex. Rice*, 402 S.W.3d at 338.

253. *Denbury Green*, 363 S.W.3d at 202.

254. *In re Tex. Rice*, 402 S.W.3d at 339.

255. *Id.* (quoting TEX. PROP. CODE ANN. § 21.021).

256. *Id.* at 339–40.



failure to make such a finding was harmless, given uncontroverted evidence in an affidavit submitted by TransCanada that its pipeline would be operated as a common carrier pipeline and that “[a]ny shipper wishing to transport crude petroleum meeting the specifications set forth in the [applicable] tariff . . . will have access to ship its crude petroleum on the pipeline for a fee[.]”<sup>257</sup>

The significance of this case is the court’s holding that the trial court erred by failing to make a preliminary finding of TransCanada’s common carrier status before issuing a writ of possession.

## VII. CONCLUSION

The title and conveyancing cases this year brought further definition to the precedents involving recurring issues, such as the conveyance of fractional royalties, property rights conveyed or reserved by implication when the instrument is silent, and common rules of construction. These should be helpful to title examiners and to draftsmen who never want to hear from title examiners. However, the most interesting case and the one with the potential to have the most significance is *Key Operating*<sup>258</sup> dealing with the implied surface easement held by the owner of the mineral estate. This easement affects basic property rights and is very important to development operations. The petition has been granted in this case, and the Texas Supreme Court has recently written extensively on the accommodation doctrine. There is a close relationship between that doctrine and the scope of the implied surface easement. Texas public policy has long favored mineral development, but increasing urbanization has brought increasing pressure on that public policy.

The sharp increase in leasing, the dramatic increase in the value of mineral rights, and the volatility in that value have produced many cases involving lease and leasing issues. Most are focused on the usual issues of royalty calculations, post-production costs, and lease perpetuation. However, a few cases really stand out. There is now clear precedent for the unacceptable level of risk that is inherent in accepting a lease provision that terminates a lease for breach of covenant. No lessee should accept such a provision. The wide spread use of contract landmen and the rush to acquire acreage has resulted in more than a little confusion in lease terms, authority to lease, and conditions to leasing. A landman clothed with apparent authority coupled with delay in promptly repudiating unacceptable terms or leases may result in a lease that the company never signed and never wanted, but nevertheless a lease that must be purchased. The overriding royalty owner has never had much protection under the law, and it now appears that in the absence of a contractual duty or a relationship duty on the lessee, the lessee is free to pursue a lessee’s own interests in washing out the overriding royalty interest in any lease renegotiation.

The risk of assigning to a weak assignee is inescapable under many operating agreements. It is not an industry practice to obtain releases from the other

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257. *Id.* at 340 (quoting affidavit of Louis Fenyvesi, director of markets and supply for TransCanada).

258. *Key Operating & Equip., Inc. v. Hegar*, 403 S.W.3d 318 (Tex. App.—Houston [1st Dist.] 201, pet. granted.).

working interest parties when an assignment is made, and not at all clear how such a release could actually be obtained. This is a material and unresolved problem under the model form operating agreements. Geologists and the purveyors of prospects in general should rejoice at the increase in protection found in recent cases for their work product. The work is valuable, and if confidentiality is maintained, it will be protected. The confidentiality agreements, nondisclosure agreements, and noncompetition agreements that the industry routinely employs, all have teeth. The trend will be to resist those agreements and to restrict their scope when it becomes a necessary risk to get a peek at the data. Although it is well established that the U.C.C. governs contracts for the purchase and sale of severed minerals, few appreciate that the course of performance can be more important in defining the rights of the parties than the written agreement.

A very significant trend in recent years has been to renew the primacy of the proceeding in trespass to try title as the proper action to resolve title issues. Because litigators have for decades defaulted to the declaratory judgment action to resolve matters in controversy, lawyers and judges are still trying cases without following the procedure mandated for trespass to try title. The opinions on appeal stretch to save the ones they can, but the litigators should by now have the message.

There seems to be some kind of organized guerilla warfare going on against pipelines. The pipelines have for years generally just rolled out their projects, but now there is widespread opposition and procedural and substantive challenges at every turn. The most common thread is an attack on common carrier status. While it seems unlikely that the ultimate power of the pipelines will be materially reduced, the exercise of that power is being strictly examined and construed.

There was not much from the Texas Supreme Court this year, but it seems like none of the parties are now willing to stop before filing a petition for review. The Supreme Court will hear only a few cases, but next year could be interesting.